IN THE

Supreme Court of the United States

OCTOBER TERM, 1962.

No. 240.

ANDRE MAXIMOV, as Trustee for the Benefit of H. ROBBIN FEDDEN, u/a dated 10/24/47,

Petitioner,

against

THE UNITED STATES OF AMERICA,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

REPLY BRIEF FOR PETITIONER.

D. NELSON ADAMS,
DAVID A. LINDSAY,
JOHN A. REED,
JOHN A. CORRY,
Attorneys for Petitioner,
1 Chase Manhattan Plaza,
New York 5, New York

Of Counsel:
DAVIS POLK WARDWELL SUNDERLAND & KIENDL,
HILL BETTS YAMAOKA FREEHILL & LONGCOPE.

INDEX.

Cases.

Treaties.

Income Tax Convention Between the United States and

IN THE

Supreme Court of the United States

OCTOBER TERM, 1962.

No. 240.

ANDRE MAXIMOV, as Trustee for the Benefit of H. ROBBIN FEDDEN, u/a dated 10/24/47,

Petitioner,

against

THE UNITED STATES OF AMERICA,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

REPLY BRIEF FOR PETITIONER.

Respondent's Point A.

Respondent does not question petitioner's position that the British beneficiaries suffered the economic burden of the tax.[1]

---

[1] Even so, he refers to the children of the grantor in our case as "contingent remaindermen" (Res. Br. p. 3) and in footnotes 1 and 2 (Res. Br. pp. 2-3) he lists contingencies as to the wife and the children, without noting that the principal contingencies, such as termination by the grantor, or the discretionary payment of principal by the trustee, would merely shift the interest in the corpus (and the retained capital gains) among a class of British beneficiaries (including the grantor) all of whom are residents of the United Kingdom. There may be a contingency as to an individual member of a family but not as to the family as a whole.

Under the Government's position, the capital gains would be taxable to the petitioner even though the trust instrument *expressly* required that the future distributions be made *only* to persons then resident in the United Kingdom.

Respondent rests his case on the premise that the term "exempt" as used in Article XIV of the Treaty means exempt only from the duty of paying the tax to the Treasury and that such term cannot mean exempt from the economic burden of the tax. In so doing he does not undertake to analyze the Treaty as a whole and altogether ignores the British effort to achieve reciprocity in terms of the economic burden of the tax. (Pet. Br. pp. 19-25.)

Respondent attempts to read domestic law into the Treaty but, under Sections 894 (26 U. S. C. §894) and 7852 (26 U. S. C. §7852) of the Internal Revenue Code of 1954, we are required to read the treaty exemption into our domestic law. (Pet. Br. pp. 36-37.) In support of his position, respondent states that under our domestic law a "trust is a separate taxable entity" (Res. Br. p. 7), "the English beneficiaries * * * are not the taxpayer" (Res. Br. p. 4) and concludes that petitioner's position "is at war with the American tax system" (Res. Br. p. 4) and "would contradict the whole scheme of trust taxation in the United States". (Res. Br. p. 10.)

Three cases are cited in the text of respondent's brief[2] in support of this charge (pp. 11-13). Two, *Biddle* v. *Commissioner*, 302 U. S. 573 (1938) and *Klein* v. *Board of Tax Supervisors*, 282 U. S. 19 (1930) (Res. Br. p. 11), involved *corporations*, not *trusts*. (Pet. Br. p. 24.) Their inapplicability to the taxation of trusts, even under domestic law, is shown by the fact that while in *Biddle* an Ameri-

[2] The only other cited cases are found in footnote 8 (Res. Br. pp. 11-12) dealing with (a) "intergovernmental immunity" cases having to do with controversial imposition of excise taxes on "cost-plus" government contractors, and income taxation of the salaries of state or federal employees, and (b) authorities relating to, in respondent's own words, "[T]heoretical economic distinctions between 'direct' and 'indirect' taxes [which] are irrelevant in the present context".

can recipient of a dividend from a British corporation was denied a credit on account of foreign income taxes paid by the corporation, an American beneficiary of a foreign trust has from the outset been allowed a credit for foreign income taxes paid by the trust.[3]

The respondent's emphasis on the *Biddle* case is particularly inapposite since the British secured its reversal in Article XIII of the Treaty. (Pet. Br. p. 24.) This assurance of reciprocity in terms of economic burden of tax in the field of corporate-stockholder relations shows the extent to which the United States acceded to the British concept in order to secure equally substantial concessions by the United Kingdom in the areas of exchange of information and foreign tax credits.

The third and last case cited in the text of respondent's brief that purports to deal with the "scheme of trust taxation in the United States" is totally irrelevant to the issue now before the Court. *Anderson* v. *Wilson*, 289 U. S. 20 (1933). (Res. Br. p. 13.)[4]

In *Anderson* v. *Wilson* this Court observed that in order to "determine whether the loss was one suffered by the trust estate, or one suffered by the taxpayer to whom the proceeds of the sale were payable, there is need at the out-

---

[3] See Section 901(b)(4) of the Internal Revenue Code of 1954, 26 U. S. C. §901(b)(4), first enacted as Section 222(a)(4) of the Revenue Act of 1918, 40 Stat. 1073. See also Section 642(a)(1) of the Internal Revenue Code of 1954, 26 U. S. C. §642(a)(1).

[4] Respondent quotes dictum from *Anderson* v. *Wilson* at page 13 of his brief, but the selected quotation contains an interesting omission. The omitted portion of the quotation, represented by asterisks in respondent's brief, reads as follows (at pp. 26-27):

> "Whether the result would be the same if the beneficiaries had been the owner of future estates in remainder, we are not required to determine. Cf. *Francis* v. *Commissioner*, 15 B. T. A. 1332, 1340. Our ruling will be kept within the limits of the case before us."

set to determine the meaning of the will". (289 U. S. 20, 24.) In the words of this Court (289 U. S. 20, 26):

> "Our answer to the inquiry as to the meaning of the will comes close to being an answer to the inquiry as to the incidence of the loss. The taxpayer has received the only legacy bequeathed to him, and received it as it was given without the abatement of a dollar. What was bequeathed was an interest in a fund to be made up when the trustees were of opinion that it would be advisable to sell. This alone was given, and this has been received."

Even assuming that the treaty exemption must be construed in light of domestic law, respondent cites no authority for his position that the exemption granted United Kingdom beneficiaries must be defeated because the domestic trust and not the English beneficiaries is "the taxpayer".

Respondent's observation that Article XIV of the Treaty "exempts *persons*, not income as such" (Res. Br. p. 7) is not relevant where the "person" is the equitable owner of the income and the trust is the "taxpayer".[5] In *Lederer* v. *Stockton*, 260 U. S. 3 (1922) the exemption of a hospital was not defeated by the interposition of a domestic

[5] Nor is petitioner's "concession" (Res. Br. pp. 5-6) that, absent Article XIV, the trust "would owe the contested tax notwithstanding that the beneficiaries are all nonresident aliens" really pertinent. Apart from the Treaty, there is no express "exemption" for nonresident aliens with respect to capital gains. Capital gains are not subject to the withholding tax provisions generally applicable to nonresident aliens because capital gains are not considered the type of income ("fixed or determinable, annual or periodical") that is subject to withholding. (See note 9, *infra*, p. 10.)

To say, as does respondent (Res. Br. p. 8), that Article XIV seems "to deal with a British resident only with respect to *his* own income and to *his* own tax liability" begs the question. The United Kingdom negotiators were primarily concerned with the burden of United States taxation and it is the beneficiaries of the trust whose interests are depleted by our capital gains tax.

trust. (Pet. Br. p. 34.) *Lederer* v. *Stockton* arose prior to the statutory allowance of a deduction in respect of income of a trust or estate "permanently set aside" for a charity (Pet. Br. p. 34), and has been cited for the proposition that "income of an estate or trust accumulated during the taxable year is deductible although it has not actually been given to a charitable organization or used directly for a charitable purpose". *Arthur Jordan Foundation* v. *Commissioner*, 210 F. 2d 885, 888 (7th Cir. 1954).

In commenting on *Lederer* v. *Stockton* in another case, Judge Augustus Hand observed that while the trustee in the *Stockton* case made "a loan of the corpus of the trust to the tax exempt remainderman," and that while this Court based its decision on the ground that the charitable organization in effect enjoyed the use of the income, the Circuit Court of Appeals below had also relied on the further ground that the remainderman "was the beneficial owner of the income." *Slocum* v. *Bowers*, 15 F. 2d 400, 403 (S. D. N. Y. 1926), *aff'd*, 20 F. 2d 350 (2d Cir. 1927).[6] Judge Hand went on to say (*ibid.*):

> "But the Supreme Court in no way disapproved of the additional ground adopted by the Court of Appeals and Chief Justice Taft, who wrote the opinion, reported in 260 U. S. 3, 43 S. Ct. 5, 67 L. Ed. 99, said: 'This residuary fund was vested in the hospital. The death of the annuitant would completely end the trust'." (At p. 403.)

---

[6] In *Slocum* v. *Bowers* Judge Augustus Hand held that undistributed income of an estate (estates and trusts are governed by the same rules) was exempt because the income was "ultimately" passed to charitable legatees, stating it is hard to believe that in the one case of administration of an estate the exemption "should turn on the technical question of whether the corporations seeking it have the legal or equitable title to the income." 15 F. 2d 400, 403. The Circuit Court of Appeals for the Second Circuit affirmed, but on other grounds, relying solely on the statutory provision, first enacted in 1918 (40 Stat. 1071) permitting a deduction for income "permanently set aside" for a charity. 20 F. 2d 350.

Fundamentally, the fact that to a limited extent a trust is "the taxpayer" under domestic law is grounded upon considerations of tax policy which are entirely different from those which form the basis of Article XIV. Our domestic laws insure that taxable income held in trust is taxed only once, either to the trust or to the beneficiary, and the liability to pay the tax equitably falls upon whichever "taxpayer" has possession of the income and hence the ability to pay the tax. The trust is not a separate taxable entity in the sense of a corporation which permits the imposition of tax twice on the same income, first in the hands of the corporation, and second in the hands of the stockholder when distributed as a dividend.

It is inconceivable that the British negotiators intended to cast an exemption accorded their residents into an ever changing morass of administrative interpretation relating to domestic law. Respondent's statement that the treaty exemption "does not purport to override our revenue laws" (Res. Br. p. 14) is particularly unpersuasive in light of his reliance on Rev. Rul. 62-154 (Res. Br. p. 8) relating to the "test for determining the residence of a trust".[7]

---

[7] As early as 1923 in I. T. 1885, II-2 Cum. Bull. 164 (1923), it was stated that the residence of a trust has nothing to do with the citizenship or residence of the trustee. On the other hand, in *B. W. Jones Trust* v. *Commissioner*, 132 F. 2d 914 (4th Cir. 1943) the Commissioner successfully contended that the residence in the United States of one of four trustees, who had possession of most of the trust assets, was itself sufficient to render the trust, established by a British subject for British beneficiaries, taxable as a United States resident. Confusion on this subject persists, as shown in Rev. Rul. 62-154.

The Court will be able to gauge the extent of "morass" in this area, from the following language in Rev. Rul. 62-154, Int. Rev. Bull. 1962-38, at 8:

> "The question was asked because I. T. 1885, C. B. II-2, 164 (1923), which was referred to in Revenue Ruling 57-245 in support of the Service position, was modified by Revenue Ruling 60-181, C. B. 1960-1, 257, and because the result

Nevertheless, respondent finds "reference" to our domestic law "permissible" under Article II(3) of the Treaty. (Res. Br. p. 14.) Article II(3) deals with the definition of terms and not with substantive provisions of the Treaty. In view of the incorporation of the treaty exemption in Section 894 of the Internal Revenue Code and the express deference in Article II(3) to the "context" of the Treaty it is inappropriate to construe the treaty exemption in terms of the technical concept of a trust as the "taxpayer". In following the British lead and placing the laws on a reciprocal basis within the Treaty (Pet. Br. p. 21), the parties fashioned substantive provisions which focus on tax burdens and disregard the legal incidence of the tax and the technical identity of the *pro forma* taxpayer. (Pet. Br. pp. 19-25.) Article XIV has the sole function and purpose of accomplishing reciprocity of tax treatment, and if reciprocity is to be accorded to capital gains, the word "exempt" must embrace in its meaning the type of exemption which it is designed to reciprocate, namely, the same relief from tax in the United States as is accorded to capital gains in the United Kingdom. (Pet. Br. pp. 13-14.) This is the context in which Article XIV must be interpreted, and this is the context which stamps "exempt" with its meaning: release from the burden of taxation.

Respondent's Point B.

Respondent has virtually abandoned the treaty analysis on which the Court below based its decision and retreats to an altogether different line of defense.

---

reached in Revenue Ruling 58-232 appears inconsistent with such modification of I. T. 1885."

Rev. Rul. 62-154 modified Rev. Rul. 57-245 and superseded Rev. Rul. 58-232.

Thus, respondent now relies on the "controversy over the taxation of nonresident aliens" (Res. Br. p. 16) and the "climate of growing hostility toward exemption for nonresident aliens". (Res. Br. p. 5.) However, respondent failed to reveal to this Court the nature of this "controversy" or the cause of the "hostility".

The hostility was directed exclusively at wealthy "refugees" who had been "making large sums of money trading on our stock exchanges", and who were physically present in the United States but were treated as nonresidents under the Internal Revenue Code and its administrative and judicial interpretation.

The fourth objection stated in the memorandum prepared by the Committee on Foreign Relations states:

> "Thus refugees who are not residents of the United States have been making large sums of money trading on our stock exchanges. The convention not only continues this existing practice but enlarges the exemption to apply to any British resident who does not have a permanent establishment in the United States." S. Exec. D, 79th Cong., 1st Sess. 25-26, 2 Legislative History of U. S. Tax Conventions (hereinafter cited as 2 Leg. Hist.) 2591-2592.

In part answer to this objection, again referring to "gains realized in the United States by a nonresident alien individual by reason of war conditions who has brought his capital into the United States and is actually living there for an indefinite period of time", the same memorandum states:

> "The tax situation presented by such aliens finds no parallel in the casual business visitor from the United Kingdom, who in the normal pursuit of his business or profession visits the United States for a short period of time. * * * Obviously, there are few,

if any, British refugees." S. Exec. D, 79th Cong., 1st Sess. 27, 2 Leg. Hist. 2593.

Testifying on the same subject, Mr. Stam pointed out that the matter was being investigated by the Internal Revenue Service (S. Exec. Rept. No. 6, 79th Cong., 1st Sess. 4, 2 Leg. Hist. 2654) and the Report of the Senate Finance Committee states:

> "* * * the subcommittee is aware of the fact that the Bureau of Internal Revenue has under active investigation the taxation of capital transactions of refugee aliens in the United States and the possibility of legislation, if found necessary, to supplement such program." S. Exec. Rept. No. 6, 79th Cong., 1st Sess. 4, 2 Leg. Hist. 2654.

Again the only respect in which the supplemental hearings considered the capital gains question was in connection with the taxation of war refugees, and a report on this subject prepared by Mr. Eldon King was submitted and is set forth in Hearings on the Income and Estate Tax Conventions Before a Subcommittee of the Committee on Foreign Relations of the United States Senate, 79th Cong., 1st Sess. 116-120, S. Exec. Rept. No. 4, 79th Cong., 2d Sess. 4-8, 2 Leg. Hist. 2712-2716, 2724-2728.

The "hostility" to the transient alien problem culminated in the enactment of Section 213 of the Revenue Act of 1950 (64 Stat. 906),* which taxed certain capital gains realized by nonresident aliens "temporarily present in the United States". The problem, nevertheless, was considered to have "no parallel in the casual business visitor from the United Kingdom" (S. Exec. D, 79th Cong., 1st

*Now Section 871 (a) of the Internal Revenue Code of 1954, 26 U. S. C. §871 (a).

Sess. 27, 2 Leg. Hist. 2593) and has no bearing whatsoever on the issue in this case.

In view of the "climate of hostility" with respect to refugees physically present in the United States and more especially in view of the language of the Treasury Regulations under Article XIV, it is clear that "assurances" to the effect that the British Treaty did not accord broader relief from capital gains tax than the earlier treaties were made in the context of nonresident aliens "temporarily present in the United States".

Respondent's leap to the conclusion that Article XIV in other respects "accorded British citizens and residents no greater relief" than was accorded by the earlier treaties (Res. Br. pp. 20-21) is demonstrably wrong. As shown in our opening brief (Pet. Br. pp. 18-19), the earlier treaties with Sweden (Art. IX, 54 Stat. 1764), France (Art. 11, 59 Stat. 899) and Canada (Art. VIII, 56 Stat. 1402) conferred an exemption only with respect to gains derived from the sale or exchange of capital assets "by" the qualifying foreign resident. Reflecting this difference in language, the Treasury Regulations under each of the treaties infer that the United Kingdom Treaty is the only treaty in which exemption from the United States capital gains tax applies where the property sold is sold "by" a domestic trust.[9]

[9] Section 7.514 of T. D. 5569, 1947-2 Cum. Bull. 190, 26 C. F. R. §507.103, which purports to permit a trust beneficiary to claim exemption from tax *under the Treaty*, albeit apparently limited to distributable gains (Pet. Br. p. 39), has no counterpart in the prior treaties (Canada T. D. 5206, 1943 Cum. Bull. 526, 26 C. F. R. §519, France T. D. 5499, 1946-1 Cum. Bull 134, 26 C. F. R. §514, Sweden T. D. 4975, 1940-2 Cum. Bull. 43, 26 C. F. R. §520). Since capital gains are not subject to the withholding tax provisions generally applicable to nonresident aliens, not being "fixed or determinable, annual or periodical" income (See Section 871 of the Internal Revenue Code of 1954, 26 U. S. C. §871), the difference under the treaties has application only under §213 of the Revenue Act of 1950 (p. 9, *supra*) which subjects nonresident aliens

The sole issue raised in this case relates only to the *extent* of the exemption accorded by the Treaty, that is to say, whether it applies only to a beneficiary to whom gains are currently distributable.

The admitted application of Article XIV to distributable gains from the sale of property held in a domestic trust, in contrast to more restrictive rules under prior treaties, is necessarily based on the broad language in which Article XIV is cast. Since the only basis for exempting *any* gain in a domestic trust is the broad language of Article XIV, and not our domestic law, there is no possible basis for distinguishing between distributed and undistributed gains or between income beneficiaries and remaindermen.

It is patently in error to say (Res. Br. pp. 21-22) that Article II(1)(g) "accomplishes the explicit saving clause found in all prior treaties". As stated by the Tax Court, the saving clause provision in the Swedish Treaty assures that "each specific item of income is made subject to tax in one or the other of the two countries" and does "not exempt a class of income from taxation by both of the contracting states." *Lewenhaupt* v. *Commissioner*, 20 T. C. 151, 160 (1953), *aff'd per curiam,* 221 F. 2d 227 (9th Cir.

---

temporarily present in the country to capital gains tax unless exempt by treaty.

In this connection, in Point C of his brief, respondent states (p. 24) that the Treasury Regulations interpret the Treaty "as exempting capital gains resulting from sales or exchanges *'by'* a British resident—not gains realized by someone else *for the eventual benefit* of a British resident" (emphasis respondent's). This language, while presumably appropriate only when applied in the case of property directly owned by a resident of the United Kingdom, reflects the distinctly different language of the three earlier treaties. Literally applied, respondent's argument here would mean that no gain from the sale of property sold "by" a domestic trust can be exempt under the Treaty, even though the gains are distributable within the taxable year of the sale. This contradicts the Government's position that the Treaty applies to distributable gains from the sale of property "by" a domestic trust.

1955). The Tax Court observed (at pp. 160-161) that Article XIV of the Swedish Convention (54 Stat. 1767), which contained both the tax credit provision and the saving clause, "was made the key provision by means of which most of the articles dealing with the avoidance of double taxation with respect to specific items of income were rendered possible." The Ninth Circuit in *American Trust Company* v. *Smyth*, 247 F. 2d 149 (1957) noted the significance of the absence of a "saving clause" in the British Convention, stating (at 154):

> "Its omission from the United Kingdom Treaty is further evidence of a purpose to exempt completely income from capital gains belonging to residents of the United Kingdom, regardless of where lodged between the time of receipt and distribution."

The coupling of the saving clause with a tax credit provision adequately serves the purpose of eliminating double taxation but could vitiate reciprocal exemptions.[10]

"Plainly," states respondent (p. 23) "the Convention was addressed to *inter*-national problems; it was not meant to disturb the structure of American tax law as it affects American income of resident American taxpayers." Yet this is precisely what the reversal of the *Biddle* case by

[10] For example, Article X of the Treaty exempts salary from United States tax if paid by the Government of the United Kingdom to a citizen of the United States who is also British. A saving clause would vitiate this provision. Similarly, Article XVI of the Treaty exempts the United Kingdom corporation *inter alia* from United States tax on its accumulated income, with reference to the surtax on unreasonable accumulation of income. This tax would ordinarily apply only in the case of a British corporation carrying on business in the United States and therefore treated under our domestic tax law as a "resident" foreign corporation. It is the overriding quality of the saving clause which no doubt offended the British and made its omission essential, in order to achieve the aim of the British negotiators in placing the tax systems on a reciprocal basis.

Article XIII accomplished. Article XIII revised the structure of the American tax credit for resident American taxpayers solely for United States tax purposes. This aspect of Article XIII is no more "*inter*-national" than the application of the Article XIV exemption to British beneficiaries, and the application of Article XIV is no more or less "*inter*-national" with respect to British income beneficiaries than it is with respect to British remaindermen.

In concluding that "the true goal of the Convention as the proclamation which precedes it announces * * * was 'the avoidance of double taxation and the prevention of fiscal evasion,' altogether foreign to this case," respondent for the first and only time echoes in one sentence the detailed analysis of the Court below, an analysis which in the context of Article XIV and other substantive provisions is demonstrably fallacious. (See Pet. Br. pp. 19-25.) Avoidance of double taxation and the prevention of fiscal evasion were, of course, important objectives from the standpoint of the United States negotiators. Indeed, they were so important that it was necessary to accept the British price of placing the laws on a reciprocal basis with mutual exemptions at the source before joining in a plan for reciprocal enforcement. (Pet. Br. pp. 20-21.) Our goal having been achieved only at the price of important concessions, the concessions made should not be lightly brushed aside.

Respondent's Point C.

In quoting Section 7.519 of the Regulations, T. D. 5569, 1947-2 Cum. Bull. 100, Section 7.519(e), 26 C. F. R. 507.108(c), dealing with beneficiaries of an estate or trust, at page 25 of his brief and his appendix (p. 30), respondent substitutes asterisks for language that makes the regulations patently defective on their face. (Pet. Br. pp. 39-40.)

That part of the regulations, relating to gains resulting from sales or exchanges "by" a British resident, deals with the wrong treaty language. (Res. Br. p. 24; Pet. Br. p. 41; See n. 9, p. 10, *supra*.)

It is a somewhat desperate maneuver to suggest that the Treasury Regulations were "approved" by the British Government. (Res. Br. p. 26.) Surely respondent does not suggest that the British negotiators approved that part of the Regulations which respondent in effect concedes is defective. (Res. Br. p. 25, n. 34; See Pet. Br. pp. 39-40.) The Regulations expressly state that a resident of the United Kingdom who is a beneficiary of a domestic trust shall be entitled to the exemption provided in Article XIV with respect to capital gains to the extent included in his "distributive share"[11] of income of such trust "if he is

[11] The term "distributive share" is somewhat blind. It is not a term used under the provisions of the Internal Revenue Code of 1939 or 1954 relating to the taxation of trust income. The Code provisions speak in terms of "distributable income" and "income which is distributed currently" (Section 162 of the Internal Revenue Code of 1939, 53 Stat. 66 as amended 1942, 56 Stat. 809) and "income required to be distributed currently" and "distributable net income". (Sections 651 and 643 of the Internal Revenue Code of 1954, 26 U. S. C. §§651, 643.) There is no statutory reference to "distributive share", except in the Code provisions relating to the taxation of partnerships. (Section 704 of the Internal Revenue Code of 1954, 26 U. S. C. §704.) As a term of art a "distributive share" of partnership income includes delayed distributions—no matter how long delayed. The regulations dealing with the "transferee liability" of beneficiaries of an estate or trust do speak in terms of the ultimate liability for unpaid taxes on the part of "distributees" to the extent of their "distributive shares", which ordinarily has reference to heirs, devisees, legatees, and remaindermen of trusts. (Treas. Regulations 111, Sec. 29.162-1.) Thus, the term "distributive share" would not appear conclusive on the question of the timing of the distribution, that is to say, whether it refers only to distributed gains or gains retained for future distribution. Respondent assumes a great deal in his reliance on "approval" by the British of this confusing, inept provision in the Regulations.

taxable in the United Kingdom on such income". If this had been read and understood by the British negotiators, they would have realized at a glance that the United Kingdom resident beneficiary would not be "taxable in the United Kingdom on such income" and therefore under the literal words of the Regulation would not qualify for the exemption under Article XIV.[12] Any "simultaneous" issuance of American and British regulations is meaningless since the British have no regulations under Article XIV.

It is incredible to state that "the Regulations have survived to this day without objection". (Res. Br. p. 26.) The Treaty was proclaimed by the President on July 30, 1946, and entered into force as of July 25, 1946, the date of exchange of instruments of ratification. (Res. Br. p. 16, n. 13). *American Trust Company* v. *Smyth, supra,* p. 12, held that Article XIV applied where all the beneficiaries, income beneficiaries and remaindermen alike, were residents of the United Kingdom and the gains were retained for future distribution in a domestic trust. The gains involved in *American Trust Company* v. *Smyth* were derived from the sale of property in 1946. 247 F. 2d at 151. Thus, the Government's interpretation of the Regulations was successfully challenged with respect to gains realized in the first year governed by this Treaty.

---

[12] The requirement "if he is taxable in the United Kingdom on such income" is not necessarily unintentional in that it reflects the philosophy of some earlier conventions. It would certainly be appropriate under the Tax Court's interpretation of the Swedish Convention where an effort was made to avoid double taxation without according a complete exemption in both contracting states. See discussion of *Lewenhaupt* v. *Commissioner,* at pp. 11-12, *supra.*

Conclusion.

For the reasons stated in our main brief and above, the judgment of the Court of Appeals should be reversed and the decision of the District Court affirmed.

Respectfully submitted,

D. Nelson Adams,
David A. Lindsay,
John A. Reed,
John A. Corry,
Attorneys for Petitioner
1 Chase Manhattan Plaza
New York 5, New York

Of Counsel:

Davis Polk Wardwell Sunderland & Kiendl
Hill Betts Yamaoka Freehill & Longcope

March 19, 1963.